

## SECURITIES AND EXCHANGE COMMISSION

### 17 CFR Parts 230, 239, and 274

[Release Nos. 33-7196; IC-21216; S7-21-95]

RIN 3235-AG55

### Money Market Fund Prospectuses

**AGENCY:** Securities and Exchange Commission.

**ACTION:** Proposed amendments to rules, forms, and staff Guides.

**SUMMARY:** The Commission is proposing amendments to the registration forms for money market funds. The amendments would tailor the prospectus disclosure requirements to the unique characteristics of money market funds. These changes are intended to allow money market funds to prepare prospectuses that are shorter, simpler, more informative, and more readily understandable to investors.

**DATES:** Comments on the proposed rule and form amendments and on the proposed staff Guides must be received on or before September 27, 1995.

**ADDRESSES:** Comments should be submitted in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549. All comment letters should refer to File No. S7-21-95. All comments received will be available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, NW., Washington, DC 20549.

**FOR FURTHER INFORMATION CONTACT:** Martha H. Platt, Senior Attorney, or Robert E. Plaze, Assistant Director, (202) 942-0721, Office of Disclosure and Investment Adviser Regulation; for accounting questions, contact James F. Volk, Assistant Chief Accountant, (202) 942-0637, Division of Investment Management, 450 Fifth Street, NW., Washington, DC 20549.

**SUPPLEMENTARY INFORMATION:** The Securities and Exchange Commission ("the Commission") today is proposing for comment amendments to Form N-1A [17 CFR 239.15A and 274.11A] and Form N-3 [17 CFR 239.17a and 274.11b], the registration forms used by open-end management investment companies ("mutual funds") and separate accounts organized as management investment companies ("separate accounts") to comply with the registration statement requirements of the Investment Company Act of 1940 [15 U.S.C. 80a-1 *et seq.*] ("1940 Act") and to register their securities under the

Securities Act of 1933 [15 U.S.C. 77a *et seq.*] ("1933 Act"). The proposed amendments would shorten and simplify money market fund prospectuses. The Commission is proposing additional amendments to Form N-1A that would: (1) modify the manner in which the yield of a tax exempt money market fund is calculated; (2) change the calculation of total return for partial years in the financial highlights table; (3) remove the requirement that funds file a schedule of performance quotation computations; and (4) amend the instructions regarding the fee table. Conforming amendments are being proposed to rule 482 under the 1933 Act [17 CFR 230.482] and Form N-2 [17 CFR 239.14 and 274.11a-1], the registration form for closed-end management investment companies. The Commission also is publishing related changes to staff Guides to Forms N-1A and N-3.

### Table of Contents

#### Executive Summary

- I. Background and Summary of Proposed Amendments
  - II. Discussion of the Proposed Amendments
    - A. Proposed Revisions Pertaining to Money Fund Prospectuses
      1. Replacement of Financial Highlights Table
      2. Descriptions of Investment Policies and Techniques
      3. Inclusion of Description of Advertised Performance Data in SAI
      4. Summary Description of Securities Valuation
    - B. Other Amendments
      1. Calculation of Tax Exempt Money Fund Yield
      2. Total Return Calculation
      3. Amendments to Fee Table
      4. Exhibit 16 to Form N-1A
    - C. Request for Comments Regarding Prospectus Simplification Generally
  - III. Amendments to Staff Guides
  - IV. Transition Period
  - V. General Request for Comments
  - VI. Cost/Benefit of Proposal
  - VII. Summary of Initial Regulatory Flexibility Analysis
- Text of Proposed Rule and Form Amendments

### Executive Summary

The Commission is proposing to amend the prospectus disclosure requirements of Form N-1A to permit and encourage money market funds ("money funds") to provide shorter prospectuses that are more relevant to the needs of typical money fund investors. The Commission believes that the proposed rule and form amendments will significantly shorten and simplify money fund prospectuses and provide valuable information to investors in more useable formats. The

most significant of the proposed changes are summarized below.

First, the multi-line financial highlights table would be replaced with a bar graph showing a fund's total returns for each of the last ten years. The bar graph is intended to provide investors with information regarding fund performance in a simple, graphic format that is easy to understand.

Second, a money fund's description of its portfolio and investment techniques would be greatly abbreviated. Money fund prospectuses often contain detailed, technical descriptions of instruments and investment techniques that are unlikely to assist an investor in understanding a money fund's essential characteristics. The Commission is concerned that these complicated descriptions add substantial length and complexity to money fund prospectuses, which may discourage investors from reading important information in the prospectuses. The Commission proposes to address this concern by permitting all money funds to describe themselves in their prospectuses with very basic, general statements about their investment objectives and portfolio composition.

The narrative disclosure that money funds would remove from their prospectuses in response to the proposals described above would be relocated to the Statement of Additional Information ("SAI"), which is available to investors upon request and without charge.

### I. Background and Summary of Proposed Amendments

Money funds are open-end management investment companies that invest in short-term debt instruments or instruments that have similar characteristics. Money funds currently hold over \$692 billion in assets<sup>1</sup> in approximately 25 million shareholder accounts.<sup>2</sup> Through these funds, individual investors are able to participate in the money markets.

Like other mutual funds, money funds offer investors a diversified and professionally managed portfolio of securities. Many investors select money funds as part of their investment plans because these funds have characteristics that allow them to be used as a cash management tool. These characteristics

<sup>1</sup> Money Fund Report (July 7, 1995). \$574 billion is invested in taxable funds and \$118 billion is invested in tax exempt funds. *Id.*

<sup>2</sup> Investment Company Institute Mutual Fund Fact Book 99 (35th ed. 1995). See Investment Company Act Rel. No. 17589 (July 17, 1990) [55 FR 30239 (July 25, 1990)] at nn. 3-7 and 15-18, and accompanying text, for a summary of the development of money funds.

include relative safety of principal, a high degree of liquidity, a wide range of shareholder services (including check-writing), and maintenance of a stable net asset value, usually of \$1.00. Money funds are not protected by federal deposit insurance, and there is no guarantee that a money fund will always be able to maintain a stable net asset value.<sup>3</sup> Nevertheless, money funds' success at maintaining a stable \$1.00 share price has encouraged investors to view these funds as alternatives to bank deposit and checking accounts.<sup>4</sup>

Form N-1A is the registration form that mutual funds, including money funds, use to satisfy the registration statement requirements of the 1940 Act and to register their shares under the 1933 Act. Form N-1A permits mutual funds to provide investors with a simplified prospectus covering matters of fundamental importance about the funds. Upon request, detailed information is available in an SAI. When the Commission proposed Form N-1A in the early 1980s, money funds were relatively new, tax exempt money funds had just been introduced, and money funds invested in only a few types of relatively simple instruments.<sup>5</sup> Accordingly, few provisions of the form reflect the unique characteristics of money funds or specify the level of

disclosure appropriate for describing the many different types of instruments that now comprise money fund portfolios. As a result, although money funds are acknowledged as being the most stable and conservative mutual funds, their prospectus disclosure is often more detailed and technical than that of other mutual funds.

While detailed disclosure about investment policies and portfolio securities may be material to investors choosing among other types of funds, it may not be material to a money fund investor. Money fund investment policies and the composition of money fund portfolios are subject to much more detailed regulation under the 1940 Act and, as a result, are very similar.<sup>6</sup> While the differences among taxable money funds, tax exempt money funds, and money funds that invest only in U.S. government securities may be material to money fund investors, small differences in types of portfolio holdings that differentiate money funds within each of these groups may not be particularly important to investors, who typically select money funds on the basis of convenience, shareholder services, or yield.

Based upon these considerations, the Commission is proposing to revise the prospectus disclosure requirements for money funds to account for the unique characteristics of money funds and the regulatory structure to which they are subject. The revisions would result in shorter and more comprehensible prospectuses that are more relevant to the needs of typical money fund investors.<sup>7</sup>

## II. Discussion of the Proposed Amendments

### A. Proposed Revisions Pertaining to Money Fund Prospectuses

#### 1. Replacement of Financial Highlights Table

The financial highlights table currently required by Item 3(a) of Form

N-1A<sup>8</sup> provides summary financial information about a fund, including the fund's total return for each of the previous ten fiscal years.<sup>9</sup> Although the table provides useful information for investors in stock and bond funds generally, some of the table's items are generally not relevant to money fund investors because money funds rarely experience changes in per share net asset value or realize capital gains.

The Commission proposes to replace the financial highlights table in money fund prospectuses with a bar graph showing the fund's total return for each of its last ten fiscal years.<sup>10</sup> Because most of a money fund's return consists of dividends, the bar graph would primarily reflect the fund's annual yield. Money funds occasionally recognize capital gains as a result of the disposition of a portfolio security, which would be reflected in the bar graph as part of the fund's total return. If a fund makes capital gains distributions during the period, a footnote to the graph would state the amount of the distribution per share and indicate that the amount of the distribution is indicated in the bar graph by a shaded or otherwise distinctively marked area of the bar for each year for which such a distribution was made.<sup>11</sup> The bar graph would be accompanied by statements that: (1) Past performance is not predictive of future performance; (2) performance is primarily affected by short-term interest rates and fund expenses; and (3) more detailed information regarding performance is contained in the financial statements in the SAI.

The bar graph is intended to provide investors with a depiction of historical

<sup>8</sup> Most of the form amendments are being proposed for both Form N-1A and Form N-3. For ease of reference, citations to proposed and current form items and instructions refer to Form N-1A unless the context otherwise requires.

<sup>9</sup> The financial highlights table contains the following fourteen items: beginning net asset value; net investment income; net gains (losses); total income from investment operations; dividends from net investment income; distributions from capital gains; returns of capital; total distributions; ending net asset value; total return; total net assets; ratio of expenses to average net assets; ratio of net income to average net assets; and portfolio turnover rate. The table is required to contain information for the fund's last ten fiscal years. Item 23 of Form N-1A requires that the financial highlights information for each of the previous five fiscal years be provided in fund annual reports to shareholders.

<sup>10</sup> Proposed Item 3(b). The financial statements for the fund's previous fiscal year would continue to be required in the SAI. See Item 23 of Form N-1A. While other mutual funds currently are required to provide a performance graph and discussion of performance in their prospectuses or annual reports, money funds are exempt from those requirements of Form N-1A. See Investment Company Act Rel. No. 19382 (Apr. 6, 1993), [58 FR 19050 (Apr. 12, 1993)] ("Release 19382").

<sup>11</sup> Proposed Item 3(b) of Form N-1A.

<sup>3</sup> Item 1(a)(vi) of Form N-1A requires a money fund to disclose this fact on the cover of its prospectus.

<sup>4</sup> An exception to this historical success occurred in September 1994 when the US Government Money Market Fund, a series of Community Bankers Mutual Fund, Inc. that had invested in certain adjustable rate notes, announced that it would liquidate and distribute less than \$1.00 per share to its shareholders. See, e.g., Olaf de Senerpont Domis and Karen Talley, "Collapse of Money Fund Seen Heightening Derivatives Scrutiny," *American Banker*, Sept. 29, 1994 at 1, 3; Leslie Wayne, "For Money Market Investors, New Cautions," *N.Y. Times*, Sept. 29, 1994 at D1, D8.

<sup>5</sup> In the 1980s, these funds generally restricted their investments to short-term U.S. government securities, bank instruments, and commercial paper. See, e.g., In the Matter of Intercapital Liquid Asset Fund, Inc., *et al.*, Investment Company Act Rel. No. 10201 (Apr. 12, 1978) [43 FR 16830 (Apr. 20, 1978)] (notice of applications for exemption from section 2(a)(41) of 1940 Act and rules promulgated thereunder and order for hearing on ten related applications). By contrast, money funds today invest in a vast array of instruments, many of which have complex structures. The types of instruments available are constantly expanding in response to demand from money funds. See *infra*, Section II.A.2 of this Release. This trend is especially marked in the case of tax exempt money funds, where the demand for securities that are eligible for money fund investment has resulted in the investment banking community developing many types of new instruments. See Investment Company Act Rel. No. 19959 (Dec. 15, 1993) [58 FR 68585 (Dec. 28, 1993)] ("Release 19959") (proposing further amendments to tighten the risk-limiting conditions of rule 2a-7, 17 CFR 270.2a-7) at nn. 24-25 and accompanying text. All references to rule 2a-7 or any paragraph of the rule will be to 17 CFR 270.2a-7.

<sup>6</sup> Rule 2a-7 [17 CFR 270.2a-7] allows money funds to use the amortized cost method of valuation and the penny-rounding method of share pricing to assist in maintaining a stable share price. In addition, any investment company that holds itself out as a money fund may only invest in U.S. dollar-denominated instruments and must meet the risk-limiting conditions of rule 2a-7 regarding portfolio quality, maturity, and diversification. Paragraphs (b), (c)(2), (c)(3) and (c)(4) of rule 2a-7. These conditions limit a fund's exposure to credit, interest rate, and currency risk. All references to rule 2a-7 or any paragraph of the rule will be to 17 CFR 270.2a-7.

<sup>7</sup> In addition, shorter prospectuses would result in reduced printing and mailing costs. Those costs usually are borne by the fund and, indirectly, by fund shareholders.

fund returns in a format that is simple and understandable. The Commission is particularly concerned that investors with long-term financial goals, such as those using mutual funds to fund a retirement plan, understand that money funds provide them with substantially less of an opportunity for long-term growth than other types of mutual funds.

Comment is requested whether funds should be required to compare their performance during each of the ten years with that of an index, and, if so, what type of index should be required for the comparison. Such a comparison would permit investors to compare how the fund performed relative to alternative investments or industry averages. For example, should money funds be required to compare their total returns to changes in the Consumer Price Index, or to a securities index? In order to foster comparability among funds, should the Commission prescribe the scale of the vertical and horizontal axes of the graph and other formatting specifications?

The Commission requests comment whether money fund investors are likely to use historical performance information when selecting a money fund. Alternatively, or supplementally, should the Commission require a short-term depiction of fund yield, such as a line graph comparing the fund's yield during the last twelve months with that of an index of short-term or money funds securities. Would investors find a line graph showing recent yields useful in money fund annual and semi-annual reports to shareholders, documents that focus on the more recent financial history of the fund? Should such a graph be substituted for the current financial highlights tables in those reports?

## 2. Descriptions of Investment Policies and Techniques

Item 4(a) of Form N-1A requires a fund to describe how it proposes to achieve its investment objectives. The Commission is proposing to amend this item to reduce substantially the amount of detailed, technical information regarding investment policies, techniques, and instruments now found in money fund prospectuses. In addition, this item would be reorganized to clarify its requirements.

Item 4(a)(ii) of Form N-1A currently requires "a short description of the types of securities" in which a fund invests, as well as any "special investment practices or techniques" used by the fund in connection with those securities and "significant investment policies or techniques (such

as risk arbitrage, repurchase agreements, forward delivery contracts, investing for control or management)" that the fund uses or intends to use in the foreseeable future.<sup>12</sup> The responses to paragraphs (a) and (b) of Item 4 have become the longest and most complex section of many money fund prospectuses.<sup>13</sup> The responses often include detailed descriptions of numerous types of instruments, including U.S. Treasury bills and notes, government agency securities, short-term tranches of collateralized mortgage obligations and other types of asset-backed securities, certificates of deposit, bankers' acceptances, floating and variable rate securities, commercial paper, and repurchase and reverse repurchase agreements. The list is even longer for tax exempt money fund prospectuses, which may contain descriptions of variable rate demand notes; put bonds; general obligation bonds; bond, revenue, and tax anticipation notes; industrial development bonds; lease obligations; tax exempt commercial paper; and "synthetic" instruments, such as tender option bonds and custodial receipts. Descriptions of particular securities are often accompanied by lengthy descriptions of investment techniques, such as purchasing securities on a "when-issued" basis and acquisition of stand-by commitments.<sup>14</sup>

The following is a typical description of a portfolio security for a tax exempt money fund currently provided in response to Item 4(a):

The Fund may purchase participation interests in municipal securities that have fixed, floating or variable rates of interest. These participation interests will be purchased from financial institutions that sell undivided interests in the securities that underlie the instrument. The Fund will only purchase such an interest if: (i) the underlying securities mature in twelve months or less or the instrument includes a right to demand payment (a "demand feature"), usually exercisable within no more than seven days; (ii) the security meets certain quality standards set forth by the Fund and federal regulation; and (iii) the security is accompanied by an opinion of

<sup>12</sup> Item 4(b)(ii) (proposed instruction 3(ii) to item 4(a)) permits a fund simply to identify a practice if five percent or less of the fund's net assets are placed "at risk" by the practice. Money funds generally are not able to take advantage of this opportunity to simplify their disclosure because they require the flexibility to employ, above the five percent "at risk" level, many or all of the investment practices they describe.

<sup>13</sup> Some money funds, however, already limit those descriptions to general, basic statements about the securities in which they invest.

<sup>14</sup> Descriptions of particular types of securities (Item 4(a)(ii)(B)(1)) and various investment techniques (Item 4(a)(ii)(B)(1) and (D)) used by a fund often appear together in the same section of money market fund prospectuses.

counsel or is the subject of a ruling from the Internal Revenue Service stating that the interest earned is exempt from federal income tax.

Another tax exempt money fund describes the investment technique of purchasing municipal bonds on a "when-issued" basis, also in response to Item 4(a), as follows:

The Fund may purchase Municipal Obligations on a "when-issued" basis—the purchase of securities which are paid for and delivered beyond the normal settlement date. The Fund will generally not pay for such securities or start earning interest on them until they are received. Securities purchased on a when-issued basis are recorded as an asset and subject to changes in value based upon changes in the general level of interest rates. The Fund expects that its commitments to purchase when-issued securities will not exceed 25% of total assets, absent unusual market conditions, and that it will not commit to purchase when-issued securities beyond 45 days. The Fund does not intend to purchase when-issued securities for speculative purposes but only to further its investment objective.

To be eligible for money fund investment under rule 2a-7, the instruments described above all must be high quality and, although they may have different mechanisms for determining interest rates or maturity, all are designed to have the stability of principal and yield of short-term debt instruments. The riskiness of any particular investment technique is further limited by rule 2a-7's maturity and currency denomination conditions,<sup>15</sup> as well as the requirement that the board of directors adopt procedures designed to maintain a stable share price or net asset value.<sup>16</sup>

Because of the limitations on securities in which a money fund is permitted to invest, the particular types of securities in which a fund invests are unlikely to be an important factor for most investors when selecting a money fund.<sup>17</sup> Moreover, detailed, technical

<sup>15</sup> Rule 2a-7 limits the amount of currency risk to which money funds can be exposed by restricting their investments to U.S. dollar-denominated instruments. Paragraph (c)(3) of rule 2a-7. The rule limits the interest rate and credit risks to which money funds can be exposed by requiring that they maintain a dollar-weighted average portfolio maturity of no more than ninety days and generally invest in individual securities that have remaining maturities of no more than 397 days. Paragraph (c)(2) of rule 2a-7.

<sup>16</sup> See paragraph (c) of rule 2a-7.

<sup>17</sup> The Commission has considered whether disclosure of each type of security may provide investors with information they can use to avoid investment in money market funds investing in securities whose characteristics may threaten the fund's stable net asset value. In 1994 a number of fund advisers took steps to maintain the share values of money funds that had invested in adjustable rate securities that had interest rate adjustment formulas that did not result in the value

descriptions of instruments and investment techniques are unlikely to contribute to investor understanding of a money fund's essential characteristics. Finally, these complicated descriptions often add substantial length to money fund prospectuses, contributing to investors' perceptions that prospectuses are too complicated and discouraging them from reading the important information that is in the prospectuses.

To address these concerns, the Commission is proposing to add an instruction to Item 4 stating that it is sufficient for a money fund to describe the characteristics of the fund and its portfolio in very general and basic terms (e.g., that it seeks to maintain a stable net asset value of \$1.00 by investing in a portfolio of high-quality, short-term debt obligations issued by corporations, banks and other financial institutions), and that a listing or description of the particular instruments that the fund may purchase is not necessary.<sup>18</sup> If the fund limits investment to a group of securities or a type of issuer (e.g., to U.S. government securities), the fund would also be required to identify any other group of securities or type of issuer in which it has reserved the right to invest more than five percent of assets, unless the fund has not invested more than five percent of its assets in those securities within the past year and has no current intention of doing so in the foreseeable future.<sup>19</sup> For example, if the "XYZ U.S. Government Money Market Fund" reserves the right to invest twenty percent of its assets in corporate obligations and has invested in such securities within the past year, the fund would state that in its prospectus.

The proposed instruction is intended to encourage funds to avoid lengthy descriptions of the areas currently covered by Item 4(a) that have resulted in technical, multi-page descriptions of types of securities and investment policies and techniques. Instead, the detailed descriptions of instruments and

techniques would be placed in the SAI, where they would be available upon request to interested investors, including those who restrict their investments in mutual funds to funds that invest only in particular types of instruments.<sup>20</sup> The proposed instruction makes clear that the Commission is not proposing to eliminate from money fund prospectuses discussion of those material investment policies that distinguish one group of money funds from another.<sup>21</sup> For example, a fund would be expected to state, as appropriate, that it proposes to achieve its investment objective by investing only in Government securities, securities exempt from the income taxes of a particular state, or securities exempt from federal income taxation. The proposed instruction also makes explicit that a money fund is not required to describe the detailed investment policies that it has adopted in order to comply with rule 2a-7.<sup>22</sup>

The proposed changes should not be interpreted to suggest that the Commission believes that investment in a money fund is riskless. No substantive changes are being proposed to existing Item 4(c) (Item 4(b), as proposed to be amended), which requires a money fund to discuss "briefly the principal risk factors associated with investment" in the fund, including risk factors peculiar to the fund and those of the same fund type generally. Money funds would continue to respond to this sub-item and to Item 1(a) of Form N-1A, which requires a money fund to disclose on the cover page of its prospectus that an investment in the fund is neither insured nor guaranteed by the U.S. government and that there can be no assurance that the fund will be able to maintain a stable net asset value.<sup>23</sup> A money fund that is sold by or through a bank, or whose name is the same as, or similar to, the name of a bank that advises or sells the fund's shares, would

also continue to be required to prominently disclose on the cover page of its prospectus that shares in the fund are not deposits or obligations of, or guaranteed or endorsed by, the bank, and that the shares are not federally insured.<sup>24</sup>

### 3. Inclusion of Description of Advertised Performance Data in SAI

Item 3(c) currently requires a brief explanation in the prospectus of how the fund calculates performance data that it advertises.<sup>25</sup> Because money fund yields are calculated in a uniform manner prescribed by the Commission, an investor is unlikely to use these descriptions when evaluating advertisements by the fund. The Commission therefore proposes to permit a money fund to place its response to this item in the SAI if the response is incorporated by reference into the prospectus.<sup>26</sup> The Commission requests comment on whether this option should be made available to other mutual funds.<sup>27</sup>

### 4. Summary Description of Securities Valuation

Item 7(b) of Form N-1A requires funds to describe, among other things, the way in which the public offering price of fund shares is determined and the timing of the determination. The methodologies money funds use to calculate their net asset values are prescribed by the 1940 Act and Commission rules and are designed so that the value of each share represents the pro rata value of the assets of the fund, typically at a stabilized share

<sup>24</sup> See Letter to Registrants from Barbara J. Green, Deputy Director, Division of Investment Management (May 13, 1993).

<sup>25</sup> This disclosure provides a basis for inclusion of performance information in advertisements. Rule 482 advertisements may only include information the "substance of which" is included in the fund's statutory prospectus. For performance quotations, this requirement is met if the methodology for calculating performance is set forth in the prospectus. See Dechert, Price & Rhoads (pub. avail. Nov. 12, 1979). The Division has recommended eliminating the "substance of which" requirement (see Protecting Investors: A Half Century of Investment Company Regulation 349, Division of Investment Management, United States Securities and Exchange Commission (May 1992)), and legislation has been introduced that would eliminate the requirement (see H.R. 1495, 104th Cong., 1st Sess. § 3 (1995)).

<sup>26</sup> Proposed Instruction to Item 3(d). Because information incorporated by reference from the SAI is deemed to be included in the prospectus, the legal requirement that the substance of the information in an advertisement be contained in the statutory prospectus would be met. If adopted, the response to this item would be the only response to a prospectus item that could be incorporated by reference from the SAI.

<sup>27</sup> The Division is considering deleting the guide regarding explanations of performance data from Form N-1A (Guide 32).

of the security returning to par on the interest rate reset date as required by rule 2a-7; the adviser of one fund holding these instruments was not in a position to take steps to maintain the fund's share price. See *supra*, note 4. Under the current requirements of Form N-1A, these funds disclosed that they invest in adjustable rate instruments, but generally did not describe the terms of the interest rate adjustment formula of each instrument. Thus, even under the current rules, investors are not able to ascertain whether to avoid funds investing in inappropriate securities. Because the interest rate adjustment formulas are complicated, if the Commission were to require disclosure of the formulas, money market fund prospectuses would be considerably longer and more complex, even though most investors could not be expected to draw any conclusions as to the appropriateness of a particular adjustable rate security.

<sup>18</sup> Proposed Instruction 1 to Item 4(a).

<sup>19</sup> Proposed Instruction 1(b) to Item 4(a).

<sup>20</sup> Proposed Instruction 3 to Item 13. Requiring more detailed disclosure in the SAI also enables Commission staff to review whether the fund's stated policies and techniques comply with regulatory requirements.

<sup>21</sup> Proposed Instruction 1(b) to Item 4(a).

<sup>22</sup> The Commission also proposes to reorganize the current structure of sub-item 4(a). Several paragraphs would be redesignated as instructions to reflect their modifying the more general requirements of Item 4.

<sup>23</sup> In addition, other amendments that were proposed to Form N-1A in 1993 would require a money fund to disclose the fund's reliance on credit and liquidity enhancements from third parties when more than forty percent of the fund's portfolio consists of securities subject to such features and, for single state tax exempt money market funds, the risks associated with reduced issuer diversification and greater geographic concentration. See Release 19959, *supra* note 5 at nn. 196-197.

value of \$1.00.<sup>28</sup> The descriptions of these methodologies, which tend to be complicated, may be less important to money fund investors than the fact that the share price represents a pro rata share of the fund's net assets. Therefore, the Commission is proposing to permit money funds simply to state in the prospectus that the share price represents a pro rata share of the net assets of the fund, and to describe in the SAI the pricing method employed by the fund.<sup>29</sup>

In the case of a money fund that seeks to maintain a stable net asset value, the timing of the determination of the share price each day may not be material to an investor who will ordinarily receive the same price per share regardless of the time a payment is made or a redemption tendered.<sup>30</sup> Therefore, the Commission is proposing to relieve money funds that seek to maintain a stable net asset value from the requirement to disclose in the prospectus the timing of the determination of the offering price. This information would continue to appear in the SAI.<sup>31</sup>

## B. Other Amendments

### 1. Calculation of Tax Exempt Money Fund Yield

Tax exempt funds typically advertise a "tax free" yield. Under staff guides, a money fund that holds itself out as distributing income that is exempt from income taxation may invest up to twenty percent of its net assets in taxable securities or invest its assets so as much as twenty percent of its income

is taxable.<sup>32</sup> In addition, most tax exempt money funds reserve the authority to temporarily invest any or all of the fund's assets in taxable securities if no suitable tax-exempt securities are available. Because taxable instruments generally have higher yields than tax exempt instruments, a prospective investor may be unaware that a tax exempt fund's relatively higher yield may be the result of the inclusion of some taxable securities in its portfolio. Therefore, the Commission is proposing to revise the money fund yield formula set forth in Item 22(a) of Form N-1A to require a tax exempt fund to reduce any taxable income by a percentage equal to the highest marginal income tax rate in effect at the time the yield is quoted.<sup>33</sup> The tax-adjusted yield would represent a more accurate tax-free yield.<sup>34</sup>

### 2. Total Return Calculation

The Commission is proposing a technical amendment to the instructions regarding calculation of the total return in the financial highlights table that would apply to all management investment companies using Forms N-1A and N-2.<sup>35</sup> Instruction 11(e) to Item 3 of Form N-1A currently requires a fund to annualize total return for partial year periods. The Commission is concerned that annualization of performance based on a short period may result in a distorted performance figure that may mislead investors.<sup>36</sup> The Commission proposes to amend the instruction in Form N-1A and add an instruction to Form N-2 to require that performance for a period of less than twelve months be stated without annualization.

### 3. Amendments to Fee Table

The Commission is proposing several technical amendments to Item 2 of Form N-1A, which requires a fund to provide in its prospectus a table summarizing the transaction and operating expenses associated with an investment in the

fund. In addition, the fee table provides examples of what expenses a shareholder would pay if shares were redeemed at the end of several time periods.

Instruction 13(a) to Item 2(a) of Form N-1A instructs funds that have expense reimbursement or fee waiver arrangements that reduce fund operating expenses to reflect these arrangements in their fee table if the reimbursement or waiver "will continue." The Commission is proposing to amend the instruction to clarify that the phrase "will continue" applies regardless of whether a guarantee that the arrangement will continue is in place. A fund is required to update its prospectus by means of a prospectus supplement or "sticker" to reflect a material change in the reimbursement or waiver arrangement.<sup>37</sup> As a result, fund shareholders will be informed of decreases in amounts reimbursed or fees waived that would have a material effect on fund expenses.

Two amendments are being proposed to conform Form N-1A to Forms N-3 and N-4. The instructions to the example in the table would be amended to permit a new fund to adjust the data in the example to reflect the completion of amortization of expenses associated with organizing the fund<sup>38</sup> and to prescribe a method for allocating account fees charged to shareholders in an investment company complex or a series company.<sup>39</sup>

Funds are currently required to provide a brief explanation of the table immediately after the table. The proposed amended instruction would permit funds to provide the explanation "contiguous to" the table, giving funds additional discretion to determine how the table's purposes can be made clear to investors.<sup>40</sup>

### 4. Exhibit 16 to Form N-1A

Funds are currently required by Item 24 of Form N-1A to include as an exhibit to their financial statements a schedule showing how the fund computes performance quotations. The Commission is proposing to remove this requirement. Funds' calculations of their performance data instead will be reviewed during fund examinations.

<sup>28</sup> The methodologies include amortized cost (acquisition cost as adjusted for amortization of premium or accretion of discount), market value (marking to market daily), and fair value (good faith estimate by the board of directors) and combinations of these methods.

<sup>29</sup> See Item 19, Instruction 1 (valuation procedure). Money market funds would continue to state in the prospectus when the fund will not process requests to purchase or sell shares. See Guide 28 to Form N-1A (interpreting Item 7 regarding days on which fund will not price shares).

<sup>30</sup> Perhaps more important to a money market fund investor is the relationship of the timing of a share purchase to the accrual of dividends on the investment (for example, whether dividends on shares begin to accrue on the day the fund receives the investment, or on the next business day). This information would continue to be required in the prospectus in response to Item 6(f) (Capital Stock and Other Securities). Funds also would be required to disclose the date on which dividends cease accruing as the result of a redemption. Proposed Instruction to Item 8(a) (Redemption and Repurchase).

<sup>31</sup> See Item 19, Instruction 3 (timing of calculation of net asset value). A money market fund that does not maintain a stable net asset value would continue to describe the timing of its share price calculation in the prospectus.

<sup>32</sup> See Guide 1 to Form N-1A.

<sup>33</sup> If a fund represents itself as being free from state and/or local income taxation as well as federal income taxation, the fund would also be required to reduce the yield of those securities that are not exempt from state and/or local income taxation by the highest marginal state and/or local income tax rates for individuals.

<sup>34</sup> The Commission is also proposing technical amendments to rule 482 and Form N-1A to clarify that money market funds may advertise tax equivalent and tax equivalent effective yields and how those yields should be calculated.

<sup>35</sup> If the proposed amendments to Item 3 are adopted, money market funds would be exempt from the Financial Highlights table requirement.

<sup>36</sup> Notwithstanding the current instruction, the Commission urges funds not to annualize the total return for a partial year.

<sup>37</sup> The Commission acknowledges that a material change requiring a sticking of a fund's prospectus would ordinarily not occur where a fee waiver or reimbursement is increased, thereby reducing fund expenses.

<sup>38</sup> Instruction 14(a) to Form N-1A.

<sup>39</sup> Proposed Instruction 14(i) to Item 2(a) of Form N-1A.

<sup>40</sup> See General Instruction 1 to Item 2, as proposed to be amended.

### *C. Request for Comments Regarding Prospectus Simplification Generally*

The Commission is currently reviewing the prospectus disclosure requirements for all management investment companies to determine what changes might improve further the quality of prospectus disclosure, particularly in light of regulatory developments and changes in the investment company industry.<sup>41</sup> The Commission would consider proposing further amendments to Form N-1A to simplify and generally improve the quality of prospectus disclosure to investors in other types of mutual funds. The Commission requests comments and suggestions about ways in which the Form may be amended to further shorten and simplify prospectus disclosure for other mutual funds. Specifically, the Commission seeks comment on: (i) whether some information currently required to be presented in narrative form could be presented more effectively in a graphic, pictorial, or tabular format; and (ii) whether the appropriate allocation of required disclosure between the prospectus and the SAI should be clarified.

The Commission also requests comment on the utility to investors of money fund portfolio schedules, which are provided in semi-annual reports to shareholders.<sup>42</sup> Do these schedules provide useful information for investors? Should other information be provided instead or in a different format from that currently required?

### **III. Amendments to Staff Guides**

Form N-1A is accompanied by a series of staff guides designed, among other things, to clarify the disclosure requirements in the form. The Appendix to this release contains draft revisions to the current guides.

The Division of Investment Management (the "Division") intends to revise Guides 3, 4, 8 and 22 to Form N-1A to reflect the amendments proposed today. Guide 3 (Investment Objectives and Policies) would be revised to urge money funds to be concise in describing the manner in which they propose to

achieve their investment objectives and would state that a general description of the types of instruments in which the fund may invest and the issuers of those instruments generally should be sufficient; that listing or describing each type of instrument in which the fund may invest is not required; and that detailed descriptions of rule 2a-7's requirements and the various nationally recognized statistical rating organizations ("NRSROs") and the ratings they assign should be omitted. The Division staff intends to revise Guide 4 (Types of Securities) to state that money funds are not required to list or describe the particular instruments in which the fund may invest. Guide 8 (Senior Securities, Reverse Repurchase Agreements, Firm Commitment Agreements and Standby Commitment Agreements) would be revised to state that money funds should discuss the use of certain trading practices in the SAI in response to Item 13 rather than in the prospectus. Finally, Guide 22 (Government Securities) would be amended to shift some of the disclosure money funds place in their prospectuses about U.S. Government securities to the SAI.

The Division also intends to revise Guides 4 and 5 to clarify certain other matters applicable to money funds. Guide 4 (Types of Securities) would be revised to clarify the Commission's policy that money funds may not invest more than ten percent of their assets in illiquid securities.<sup>43</sup> Guide 5 (Portfolio Turnover) would be amended to indicate that money funds need not discuss the effects of portfolio turnover, as an investment technique, in the prospectus. Money funds would still be required to discuss the effects of portfolio turnover in the SAI.<sup>44</sup>

The Division requests comment on the proposed changes to the guides and the deletion of the guides regarding performance data,<sup>45</sup> as well as any suggestions for amendment of existing guides that would result in improved

disclosure by money funds and other types of mutual funds.

### **IV. Transition Period**

If adopted, the proposed amendments would become effective sixty days after publication in the **Federal Register**. Funds would be required to conform their prospectuses and SAIs to the amendments in their next post-effective amendment filed after the conclusion of the sixty day period that updates financial statements pursuant to the requirements of section 10(a)(3) of the 1933 Act [15 U.S.C. 77j(a)(3)]. New funds would be required to implement the new requirements in registration statements filed after the conclusion of the sixty day period.

### **V. General Request for Comments**

All interested persons who wish to submit written comments on the proposed form, rule, and Guide amendments discussed in this release, to suggest other amendments to Forms N-1A and N-3, or to comment on related matters that might have a significant impact upon the proposals discussed in this release, are requested to do so. Commenters suggesting alternative approaches are encouraged to submit proposed text to amend the Form or related rules or staff guides.

### **VI. Cost/Benefit of Proposal**

The changes to Forms N-1A and N-3 and related rules proposed today are intended to shorten and simplify the prospectuses provided to investors and potential investors in money funds and to improve the quality of prospectus disclosure by these funds. The proposed revisions should benefit investors by providing them with a shorter, clearer and, therefore, more useful document and better enable investors to make an informed investment decision. Because the proposed revisions would shorten the prospectuses provided by most money funds, the revisions should reduce the burdens of preparing and the cost of mailing the prospectus for funds. That information which is transferred from the prospectus to the SAI will lengthen the SAIs of some funds; however, the number of investors typically requesting the SAI is much lower than the number of investors to whom the prospectus will be provided. The Commission is interested in any public comment concerning the cost savings or cost burdens to money funds of all sizes affected by these proposals.

### **VII. Summary of Initial Regulatory Flexibility Analysis**

The Commission has prepared an Initial Regulatory Flexibility Analysis in

<sup>41</sup> The Commission recently issued a concept release regarding mutual fund risk disclosure and requested comment regarding a broad range of issues related to this topic. See Investment Company Act Rel. No. 20974 (Mar. 29, 1995) [60 FR 17172 (Apr. 4, 1995)].

<sup>42</sup> Rule 30d-1 [17 CFR 270.30d-1] requires that shareholder reports contain the financial statements specified in the appropriate investment company registration statement form. Instructions for preparing financial statements are contained in the registration statement forms, which refer to the requirements of Regulation S-X. See, e.g., instructions to Item 23 of Form N-1A.

<sup>43</sup> See Investment Company Act Rel. No. 13380 (July 11, 1983) [48 FR 32555 (July 18, 1983)]. See also Investment Company Institute (pub. avail. Dec. 9, 1992). The limit on illiquid holdings by other types of mutual funds is fifteen percent of net assets. See Investment Company Act Rel. No. 18612 (Mar. 12, 1992). See also Merrill Lynch Money Markets, Inc. (pub. avail. Jan. 14, 1994) (subject to certain conditions, limit on illiquid securities does not apply to commercial paper issued in reliance on Section 4(2) of the 1933 Act).

<sup>44</sup> In the 1993 amendments to Form N-1A, money funds were explicitly exempted from the requirement to state their portfolio turnover rates in the Financial Highlights table. See Release 19382, *supra* note 10 at n.3.

<sup>45</sup> See *supra* note 31.

accordance with 5 U.S.C. 603 regarding the proposed amendments. The Analysis notes that the proposed amendments are intended to simplify money fund prospectus disclosure. Pertinent information contained in the preceding section of this release ("Cost/Benefit of Proposal") is also reflected in the Analysis. A copy of the Initial Regulatory Flexibility Analysis may be obtained by contacting Martha H. Platt, Mail Stop 10-6, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549.

#### Text of Proposed Rule and Form Amendments

#### List of Subjects in 17 CFR Parts 230, 239, and 274

Investment companies, Reporting and recordkeeping requirements, Securities.

For the reasons set out in the preamble, the Commission is proposing to amend Chapter II, Title 17 of the Code of Federal Regulations as follows:

#### PART 230—GENERAL RULES AND REGULATIONS, SECURITIES ACT OF 1933

1. The authority citation for Part 230 continues to read in part as follows:

**Authority:** 15 U.S.C. 77b, 77f, 77g, 77h, 77j, 77s, 77sss, 78c, 78l, 78m, 78n, 78o, 78w, 79l(d), 79t, 80a-8, 80a-29, 80a-30, and 80a-37, unless otherwise noted.

\* \* \* \* \*

2. Section 230.482 is amended by removing the word "or" at the end of paragraph (d)(1); removing the period and adding "; or" at the end of paragraph (d)(2); and adding paragraph (d)(3) to read as follows:

#### § 230.482 Advertising by an investment company as satisfying requirements of section 10.

\* \* \* \* \*

(d) \* \* \*

(3) In the case of a money market fund holding itself out as distributing income exempt from regular federal income tax, in addition to the quotation of yields described in paragraphs (d)(1) and (d)(2) of this section:

(i) A quotation of current yield described in paragraph (d)(1) of this section and a corresponding quotation of tax equivalent yield based on the method of computation prescribed in Form N-1A, relating to the same base period and of equal prominence; or

(ii) A quotation of current yield and effective yield and corresponding quotations of tax equivalent current yield and tax equivalent effective yield based on methods of computation prescribed in Form N-1A, relating to the

same base period and of equal prominence.

\* \* \* \* \*

#### PART 239—FORMS PRESCRIBED UNDER THE SECURITIES ACT OF 1933

3. The authority citation for Part 239 continues to read, in part, as follows:

**Authority:** 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 77sss, 78c, 78l, 78m, 78n, 78o(d), 78w(a), 78l(d), 79e, 79f, 79g, 79j, 79l, 79m, 79n, 79q, 79t, 80a-8, 80a-29, 80a-30 and 80a-37, unless otherwise noted.

\* \* \* \* \*

#### PART 274—FORMS PRESCRIBED UNDER THE INVESTMENT COMPANY ACT OF 1940

4. The authority citation for Part 274 continues to read as follows:

**Authority:** 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 78c(b), 78l, 78m, 78n, 78o(d), 80a-8, 80a-24, and 80a-29, unless otherwise noted.

**Note:** Form N-2 does not and the amendments will not appear in the Code of Federal Regulations.

5. Form N-2 (referenced in §§ 239.14 and 274.11a-1) is amended by removing "and" at the end of paragraph (b), removing the period at the end of paragraph (c), adding "; and" at the end of paragraph (c), and adding instruction 13.d. to Item 4.1, to read as follows:

#### Form N-2

\* \* \* \* \*

#### Item 4. Financial Highlights

##### 1. General \* \* \*

#### Instructions

##### General Instructions

\* \* \* \* \*

##### Total Investment Return

13. \* \* \*

d. for a period of less than a full fiscal year, state the total investment return for the period and disclose in a note to the table that the figure is not annualized.

\* \* \* \* \*

**Note:** Form N-1A does not and the amendments will not appear in the Code of Federal Regulations.

6. General Instruction A of Form N-1A (referenced in §§ 239.15A and 274.11A) is amended by adding a second paragraph (unnumbered) to read as follows:

#### Form N-1A

\* \* \* \* \*

#### General Instructions

##### A. Rule as to Use of Form N-1A

\* \* \* \* \*

Several Items of Form N-1A contain specific provisions or instructions for money market fund Registrants. See General Instruction E and Items 1, 3, 4, 7, and 8 of Part A, Items 13, 22 and 23 of Part B, and Item 32 of Part C. In addition, money market fund registrants need not respond to Items 5(c) and 5A.

\* \* \* \* \*

7. General Instruction E of Form N-1A (referenced in §§ 239.15A and 274.11A) is amended by removing the second sentence of the second paragraph (unnumbered) and adding two sentences to the end of that paragraph, to read as follows:

#### Form N-1A

\* \* \* \* \*

#### General Instructions

\* \* \* \* \*

#### E. Incorporation by Reference

\* \* \* \* \*

\* \* \* In general, a Registrant may incorporate by reference, in answer to any item in a registration statement filed on Form N-1A not required to be included in a prospectus, any information contained elsewhere in the registration statement or any information contained in other statements, applications or reports filed with the Commission, except that a money market fund Registrant's response to Item 3(d) may be incorporated into the prospectus by reference from the Statement. A money market fund Registrant that elects to incorporate its response to Item 3(d) from the Statement of Additional Information is not required as a result of that incorporation to physically deliver the Statement with the prospectus if the Statement is available as described in the first paragraph of this instruction.

\* \* \* \* \*

8. Item 1, Part A of Form N-1A (referenced in §§ 239.15A and 274.11A) is amended by adding an instruction immediately following paragraph (a)(iii), to read as follows:

#### Form N-1A

\* \* \* \* \*

#### Part A

#### Information Required in a Prospectus

##### Item 1. Cover Page

(a) \* \* \*

(iii) \* \* \*

#### Instruction

A money market fund Registrant incorporating by reference from the Statement of Additional Information only its response to Item 3(d) must



include within the prospectus a statement that information has been incorporated into the prospectus by reference from the Statement of Additional Information, but may omit the statement from its cover page.

9. Item 2, General Instruction 1 of Form N-1A (referenced in §§ 239.15A and 274.11A) is revised by removing "Immediately after" and adding in its place "Contiguous to".

10. Item 2, Part A of Form N-1A (referenced in §§ 239.15A and 274.11A) is amended by adding paragraph (c) instruction 13 to read as follows:

#### Form N-1A

\* \* \* \* \*

#### Part A

#### Information Required in a Prospectus

#### Item 2. Synopsis

(a)(i) \* \* \*

#### Instructions

*General Instructions* \* \* \*

*Annual Fund Operating Expenses*

\* \* \*

13. (a) \* \* \*

(c) The registrant should reflect any expense reimbursement or fee waiver arrangement that reduced any fund operating expense that is expected to continue, regardless of whether the reimbursement or waiver arrangement has been guaranteed.

11. Item 2, Part A of Form N-1A (referenced in §§ 239.15A and 274.11A) is amended by adding " , except that an appropriate adjustment to reflect reduced annual expenses from completion of organization expense amortization may be made" before the semi-colon at the end of instruction 14(a).

12. Item 2, Part A of Form N-1A (referenced in §§ 239.15A and 274.11A) is amended by adding paragraph (i) to instruction 14 to read as follows:

#### Form N-1A

\* \* \* \* \*

#### Part A

#### Information Required in a Prospectus

#### Item 2. Synopsis

(a)(i) \* \* \*

#### Instructions

*General Instructions* \* \* \*

#### Example

14. \* \* \*

(i) Reflect any administrative fee collected by dividing the total amount of the fee collected during the year by all funds or series whose shareholders are subject to the administrative fee by

the total average net assets of all the funds or series. Add the resulting percentage to "Annual Fund Operating Expenses" and assume that it remains the same in each of the one, three, five, and ten-year periods. New Registrants should estimate administrative fees collected.

13. Item 3 of Form N-1A (§§ 239.15A and 274.11A) is amended by revising the introductory text of paragraph (a) and revising instruction 11(e) to paragraph (a), redesignating paragraphs (b), (c), and (d) as paragraphs (c), (d), and (e), and adding paragraph (b) and an instruction to newly designated paragraph (d) to read as follows:

#### Form N-1A

\* \* \* \* \*

#### Item 3. Condensed Financial Information

(a) For a Registrant other than a money market fund, furnish the following information for the Registrant, or for the Registrant and its subsidiaries, consolidated as prescribed in Rule 6-03 [17 CFR 210.6-03] of Regulation S-X.

\* \* \* \* \*

#### Instructions

#### General Instructions

\* \* \* \* \*

#### Total Return

11. \* \* \*

(e) for a period of less than a full fiscal year, state the total return for the period and disclose in a note to the table that the figure is not annualized.

\* \* \* \* \*

(b) For a money market fund Registrant, provide a bar graph showing the annual total returns of the fund for each of the last ten fiscal years, or the life of the fund if less than ten years. The graph should also show the return for each year in numerical form.

Accompany the graph with a statement or statements that: (1) Past performance is not predictive of future performance; (2) money market fund performance is primarily affected by short-term interest rates and fund expenses (and provide a cross-reference to the Registrant's tabular responses to Item 2(a), unless the bar graph and tabular responses to Item 2(a) appear on the same page of the prospectus); and (3) financial statements providing more detailed information regarding the fund's performance are contained in the Statement of Additional Information.

#### Instructions

#### General

Briefly explain the nature of the information contained in the bar graph and that the information is derived from the financial statements in the Statement of Additional Information. The auditor's report as to the financial statements need not be included in the prospectus. Note that the auditor's report as to the fund's financial data reflected in the bar graph is included elsewhere in the registration statement, specify its location, and state that it can be obtained by shareholders.

#### Bar Graph Presentation

1. *Partial Years/New Registrants.* Do not reflect partial fiscal years in the bar graph. The first year shown in the graph will be the first full fiscal year for which: (i) the Registrant's registration statement was effective (or, in the case of a series, the Registrant offered shares of the series); or (ii) the Registrant (or series) invested its assets in accordance with its investment objectives.

2. *Total Return.* Calculate total return as prescribed in Instruction 11 to Item 3(a) of this form.

3. *Distribution of Capital Gains.* If the fund made capital gains distributions during the period, state in a footnote to the graph what the amount of the distribution per share was and state that such distribution is reflected in the bar graph by means of a shaded or otherwise distinctively marked area within the bar for each year in which capital gains distributions were made.

4. *Format.* Measure return on the vertical axis of the bar graph and measure time in yearly increments on the horizontal axis.

5. *Series Companies.* Treat each series as a separate Registrant for purposes of this item.

\* \* \* \* \*

(d) \* \* \*

#### Instruction

A money market fund Registrant may incorporate its response to this sub-item from the Statement of Additional Information. See General Instruction E.

\* \* \* \* \*

14. Form N-1A (referenced in §§ 239.15A and 274.11A) is amended by revising Item 4 to read as follows:

#### Form N-1A

\* \* \* \* \*

#### Item 4. General Description of Registrant

(a) Concisely discuss the organization and operation or proposed operation of the Registrant. Include the following:



(i) basic identifying information, including:

(A) the date and form of organization of the Registrant and the name of the state or other sovereign power under the laws of which it is organized; and

(B) the classification and subclassification of the Registrant pursuant to Sections 4 and 5 of the 1940 Act [15 U.S.C. 80a-4, 80a-5];

(ii) a concise description of the investment objectives and policies of the Registrant, including, if those objectives may be changed without a vote of the holders of the majority of the voting securities, a brief statement to that effect; and

(iii) a concise discussion of how the Registrant proposes to achieve such objectives, including:

(A) a short description of the types of securities in which the Registrant invests or will invest principally and, if applicable, any special investment practices or techniques that will be employed in connection with investing in such securities;

(B) if the Registrant proposes to have a policy of concentrating in a particular industry or group of industries, identification of such industry or industries;

(C) identification of any other policies of the Registrant that may not be changed without the vote of the majority of the outstanding voting securities, including those policies which the Registrant deems to be fundamental within the meaning of Section 8(b) of the 1940 Act; and

(D) a concise description of those significant investment policies or techniques (such as risk arbitrage, repurchase agreements, forward delivery contracts, investing for control or management) that are not described pursuant to subparagraphs (a)(iii) (A)-(C) above that the Registrant employs or has the current intention of employing in the foreseeable future.

#### Instructions

1. In responding to paragraph (a)(iii) of this item (other than paragraph (a)(iii)(B), regarding concentration), it is sufficient for a money market fund Registrant to: (a) describe the characteristics of the Registrant in general terms (e.g., that it seeks to maintain a stable net asset value of \$1.00 by investing in a portfolio of high quality short-term debt obligations issued by corporations, banks, and other financial institutions, etc.) without listing or describing the particular instruments in which the fund may invest or explaining detailed investment policies designed to comply with rule 2a-7 of the 1940 Act; and (b) if the fund

limits investment to a group of securities or a type of issuer (e.g., to U.S. government securities, or securities the distributions from which are exempt from federal income taxes), identify: (i) the group of securities or type of issuer and (ii) any other group of securities or type of issuer in which the fund reserves the right to invest more than 5% of its assets and state the maximum percentage of the fund's assets that may be so invested, unless the Registrant has not invested more than 5% of its assets in those securities within the past year and has no current intention of doing so in the foreseeable future.

2. "Concentration," for purposes of paragraph (a)(iii)(2), is deemed to be 25% or more of the value of the Registrant's total assets invested or proposed to be invested in a particular industry or group of industries. A fund's policy on concentration should not be inconsistent with the Registrant's name.

3. Discussion of types of investments that will not constitute the Registrant's principal portfolio emphasis, and of related policies or practices, should generally receive less emphasis in the prospectus, and under the circumstances set forth below may be omitted or limited to information necessary to identify the type of investment, policy, or practice. Specifically, and notwithstanding paragraph (a) above:

(i) If the effect of a policy is to prohibit a particular practice, or, if the policy permits a particular practice but the Registrant has not employed that practice within the past year and has no current intention of doing so in the foreseeable future, do not include disclosure as to that policy; and

(ii) If such a policy has the effect of limiting a particular practice in such a way that no more than 5% of the Registrant's net assets are at risk, or, if the Registrant has not followed that practice within the last year in such a manner that more than 5% of the Registrant's net assets were at risk, and does not have a current intention of following such practice in the foreseeable future in such a manner that more than 5% of the Registrant's net assets will be at risk, disclosure of information in the prospectus about such practice should be limited to that which is necessary to identify the practice.

(b) Discuss briefly the principal risk factors associated with investment in the Registrant, including factors peculiar to the Registrant as well as those generally attendant to investment in an investment company with

investment policies and objectives similar to the Registrant's.

\* \* \* \* \*

15. Form N-1A (referenced in §§ 239.15A and 274.11A) is amended by adding an instruction following paragraph (b) of Item 7 to read as follows:

#### Form N-1A

\* \* \* \* \*

#### Item 7. Purchase of Securities Being Offered

\* \* \* \* \*

(b) \* \* \*

#### Instruction

In responding to sub-item (b)(i), a money market fund Registrant need only state that the public offering price per share represents a proportionate interest in the net assets of the fund. In responding to sub-item (b)(ii), a money market fund Registrant that seeks to maintain a stabilized net asset value need not state the time of day at which net asset value is calculated.

\* \* \* \* \*

16. Form N-1A (referenced in §§ 239.15A and 274.11A) is amended by adding an instruction following paragraph (a) of Item 8 to read as follows:

#### Form N-1A

\* \* \* \* \*

#### Item 8. Redemption or Repurchase

(a) \* \* \*

#### Instruction

In responding to paragraph (a), a money market fund Registrant need not discuss the timing of share pricing but should state how the timing of a redemption request will affect the accrual or payment of dividends.

\* \* \* \* \*

17. Form N-1A (referenced in §§ 239.15A and 274.11A) is amended by adding an instruction 3 following paragraph (b) of Item 13 to read as follows:

#### Form N-1A

\* \* \* \* \*

#### Item 13. Investment Objectives and Policies

\* \* \* \* \*

(b) \* \* \*

#### Instructions

\* \* \* \* \*

3. In responding to this item, a money market fund Registrant should include descriptions of:

- (i) The types of instruments which it purchases or intends to purchase;
- (ii) The types of issuers that issue the instruments in which it intends to invest;
- (iii) Significant investment policies or techniques (e.g., forward delivery contracts, repurchase agreements, and standby commitments) that the Registrant employs or has the current intention of employing in the foreseeable future; and
- (iv) The quality, maturity, and diversity restrictions which pertain to money market fund investments, to the extent such descriptions are not included in the prospectus in response to Instruction 1 to Item 4.

\* \* \* \* \*

18. Form N-1A (referenced in §§ 239.15A and 274.11A) is amended by revising the introductory text of paragraph (a), redesignating paragraphs (a)(iii) and (a)(iv) as paragraphs (a)(v) and (a)(vi); adding paragraphs (a)(iii), (a)(iv), and (a)(vii); revising Instruction 4 to paragraph (a); adding Instruction 5 to paragraph (a); and revising the introductory text of paragraph (b)(iii) of Item 22 to read as follows:

#### Form N-1A

\* \* \* \* \*

#### Item 22. Calculation of Performance Data

(a) *Money Market Funds.* If a money market fund Registrant advertises a yield quotation, an effective yield quotation, a tax equivalent yield quotation, or a tax equivalent effective yield quotation, furnish:

\* \* \* \* \*

(iii) A tax equivalent current yield quotation computed by dividing that portion of the yield of the Registrant (as computed pursuant to Item 22(a)(i)) which is tax-exempt by one minus a stated income tax rate and adding the product to that portion, if any, of the yield of the Registrant that is not tax-exempt;

(iv) A tax equivalent effective yield quotation computed by dividing that portion of the effective yield of the Registrant (as computed pursuant to Item 22(a)(ii)) which is tax-exempt by one minus a stated income tax rate and adding the product to that portion, if any, of the yield of the Registrant that is not tax-exempt;

\* \* \* \* \*

(vii) The income tax rate used in the computation.

#### Instructions

\* \* \* \* \*

4. If the Registrant does not advertise any of the four types of yield, it need

not disclose or discuss the computation of that yield.

5. If the Registrant holds itself out as distributing income that is exempt from federal and/or state and/or local income taxation, in calculating yield and effective yield (but not tax equivalent yield or tax equivalent effective yield), the Registrant must reduce the yield quoted by the effect of any income taxes on the shareholder receiving dividends, employing the maximum rate for individual income taxation. For example, if the Registrant holds itself out as distributing income exempt from federal taxation and the income taxes of State A, but invests in some securities of State B, it must reduce its yield by the effect of state income taxes that must be paid by the residents of State A on that portion of the income attributable to the securities of State B.

#### (b) Other Registrants.

\* \* \* \* \*

(iii) *Tax Equivalent Yield.* If the Registrant advertises a tax equivalent yield, furnish,

\* \* \* \* \*

19. Form N-1A (referenced in §§ 239.15A and 274.11A), paragraph (b) of Item 24, is amended by removing paragraph (16) and redesignating paragraphs (17) and (18) as paragraphs (16) and (17).

20. Guide 3 to Form N-1A is revised to read as follows:

#### Guide 3. Investment Objective and Policies

In the response to Item 4, the registrant's investment objective and policies (including the types of securities in which it will invest) should be clearly and concisely stated in the prospectus so that they may be readily understood by the investor. Because the circumstances of each registrant will vary, it is not possible to define precisely what level of investment would make a particular type of investment one in which the registrant invests "principally," as that term is used in Item 4. As a general matter, however, the level of disclosure as to a particular type of investment should be consistent with the prominence of that type of investment in the registrant's portfolio. The prospectus should emphasize the main types of investments the registrant proposes to make and the principal risks inherent in such investments. Accordingly, discussions of types of investments that will not constitute the registrant's principal portfolio emphasis should be as brief as possible and, in many cases, may be limited to identifying the particular type of investments. (As

discussed below, the instructions delineate certain circumstances in which disclosure may be so limited.) Similar treatment should be accorded to other types of practices, such as borrowing money. In order to achieve the objective of clear and concise disclosure, registrants should avoid extensive legal and technical detail and need not discuss every possible contingency, such as remote risks.<sup>3</sup>

Money market fund registrants in particular are urged to be concise in describing the manner in which they propose to achieve their investment objectives (item 4(a)(iii)). A general description of the types of instruments in which the registrant may invest (i.e., short-term, high quality instruments) and the types of issuers that issue the securities in which the registrant may invest (e.g., corporations, banks, etc.) should generally be sufficient. As stated in Instruction 1 to Item 4, listing or describing each type of instrument in which the registrant may invest is not required; however, the registrant should identify those groups of securities or types of issuers in which it has reserved the right to invest more than 5% of its assets, unless it has not invested more than 5% of its assets in those securities or issuers within the past year and has no current intention of doing so in the foreseeable future. Registrants should omit detailed descriptions of rule 2a-7's requirements and the various NRSROs and the ratings they assign to securities in which the fund may or does invest. More detailed responses regarding investment policies and techniques should be provided in the Statement of Additional Information in response to Item 13.

Pursuant to Instruction 3(i) to Item 4(a), the registrant should omit from the prospectus disclosure about so-called negative investment policies, that is, policies that prohibit a particular type of investment or practice. Item 4(a) may have particular applicability to those types of activities for which section 8(b) of the 1940 Act specifically requires that there be information in the registration statement. Although Item 4(a) generally does not attempt to define what or how much disclosure should be made about particular practices, Instruction 3(ii) calls for minimal disclosure of policies registrant will not follow to a significant extent. Specifically, if not more than 5 percent of the registrant's net assets will be at risk, the prospectus should merely identify the policy or practice. For example, if a registrant planned to

<sup>3</sup> See individual subject headings of these Guidelines concerning disclosure for specific investment techniques or policies.

invest no more than 5 percent of its net assets in speculative growth stocks, it would be sufficient to state that policy in the prospectus without elaboration.

The response to Item 13 should include a fuller discussion in the Statement of Additional Information of those investment policies of the registrant with respect to which an abbreviated or no narrative description is included in the prospectus. Fuller descriptions of the registrant's principal types of investment may also be appropriate, depending on the circumstances. If the registrant has not used a policy in the past, the registrant should disclose that fact, as well as its intention with respect to that policy in the coming year in the Statement of Additional Information in responding to Item 13.

21. Guide 4 to Form N-1A is amended by adding a footnote at the end of the first sentence to read as follows:

#### Guide 4. Types of Securities

\* \* \* \* \*

<sup>4</sup> As set forth in instruction 1 to Item 4, money market fund Registrants are not required to list or describe the particular instruments in which the fund may invest.

\* \* \* \* \*

22. Guide 4 to Form N-1A is amended by adding a sentence and a footnote in the last paragraph (unnumbered) after the phrase "fifteen percent of its net assets." to read as follows:

#### Guide 4. Types of Securities

\* \* \* \* \*

\* \* \* A money market fund is limited to investing less than ten percent of its assets in illiquid securities.<sup>5</sup> \* \* \*

\* \* \* \* \*

23. Guide 5 to Form N-1A is amended by adding a footnote at the end of the first sentence to read as follows, and sequentially renumbering all subsequent footnotes in the guides to Form N-1A:

#### Guide 5. Portfolio Turnover

\* \* \* \* \*

<sup>6</sup> Money market funds are not required to discuss the effects of portfolio turnover in their prospectuses.

\* \* \* \* \*

24. Guide 8 to Form N-1A is amended by adding a sentence to the second paragraph (unnumbered) following the third sentence to read as follows:

#### Guide 8. Senior Securities, Reverse Repurchase Agreements, Firm Commitment Agreements and Standby Commitment Agreements

\* \* \* \* \*

\* \* \* Money market funds should discuss their use of these trading practices in the Statement of Additional Information in response to Item 13 (see Instruction 1 to Item 4(a)(iii) and Instruction 3 to Item 13). \* \* \*

25. Guide 22 to Form N-1A is amended to read as follows:

#### Guide 22. Government Securities

If the registrant is investing in United States Government securities, the prospectus should reflect under what conditions, and to what extent the registrant intends to invest its assets in United States Government securities.

If a registrant other than a money market fund is investing to a significant extent in United States Government securities on a routine basis, the prospectus should include the following information: (i) The types of Government securities in which the fund will invest; (ii) examples of Government agencies and instrumentalities in whose securities the fund will invest; and (iii) whether the securities of such agency or instrumentality are: (a) Supported by full faith and credit of the United States, (b) supported by the ability to borrow from the Treasury, (c) supported only by the credit of the agency or instrumentality, or (d) supported by the United States in some other way. If the registrant is a money market fund, the disclosure described in (i)-(iii) above should be placed in the Statement of Additional Information.

If the registrant is a money market fund holding itself out as investing in United States Government securities, and the registrant does not invest all of its assets in securities backed by the full faith and credit of the United States Government, the fund should not suggest in its prospectus or sales material that there is no credit risk associated with the fund's investments.

26. Guide 28 to Form N-1A is amended by removing the following phrase in the first sentence of the tenth paragraph (unnumbered): "with portfolio securities that mature in one year or less".

27. General Instruction A of Form N-3 (referenced in §§ 239.17a and 274.11b) is amended by adding a paragraph between the first and second (unnumbered) paragraphs to read as follows:

#### Form N-3

\* \* \* \* \*

#### General Instructions

##### A. Rule as to Use of Form N-3

\* \* \* \* \*

Several Items of Form N-3 contain specific provisions or instructions for money market accounts. See General Instruction G and Items 1, 4, 5, 11, 12, of Part A, Items 19 and 27 of Part B, and Item 37 of Part C.

\* \* \* \* \*

**Note:** Form N-3 does not and the amendments will not appear in the Code of Federal Regulations.

28. General Instruction G of Form N-3 (referenced in §§ 239.17a and 274.11b) is amended by removing the period and adding a comma at the end of the second paragraph (unnumbered) and adding the following to read as follows:

#### Form N-3

\* \* \* \* \*

#### General Instructions

\* \* \* \* \*

##### G. Incorporation by Reference

\* \* \* \* \*

\* \* \*, except that a Registrant's response to Item 4(d) may be incorporated into the prospectus by reference from the Statement of Additional Information. A money market account electing to incorporate its response to Item 4(d) from the Statement of Additional Information will not be required as a result of that incorporation to physically deliver the Statement with the prospectus if the Statement is available as described in the first paragraph of this instruction.

\* \* \* \* \*

29. Item 1 of Form N-3 (referenced in §§ 239.17a and 274.11b) is amended by adding an instruction at the end of paragraph (a)(vi) to read as follows:

#### Form N-3

\* \* \* \* \*

##### Item 1. Cover Page

- (a) \* \* \*  
(vi) \* \* \*

##### Instruction

A money market account incorporating by reference from the Statement of Additional Information only its response to Item 4(c) must include within the prospectus a statement that information has been incorporated into the prospectus by reference from the Statement of Additional Information, but may omit the statement from its cover page.

\* \* \* \* \*

30. Item 3 of Form N-3 (referenced in §§ 239.17a and 274.11b) is amended by

<sup>5</sup> See Investment Company Act Rel. No. 13380 (July 11, 1983), 48 FR 32555 (July 18, 1983). See also Investment Company Institute (pub. avail. Dec. 9, 1992).

revising General Instruction 1 by removing "Immediately after" and substituting in its place "Contiguous to".

31. Item 3 of Form N-3 (referenced in §§ 239.17a and 274.11b) is amended by adding paragraph (c) to instruction 18 to read as follows:

#### Form N-3

\* \* \* \* \*

#### Item 3. Synopsis

(a) \* \* \*

Annual Expenses \* \* \*

18. (a) \* \* \*

(b) \* \* \*

(c) The registrant should reflect any expense reimbursement or fee waiver arrangement that reduced any operating expense that is expected to continue, regardless of whether the reimbursement or waiver arrangement has been guaranteed.

32. Item 4 of Form N-3 (referenced in §§ 239.17a and 274.11b) is amended by revising the introductory text of paragraph (a), redesignating paragraphs (b), (c), and (d) as paragraphs (c), (d), and (e), adding paragraph (b), and adding an instruction to newly designated paragraph (d) to read as follows:

#### Form N-3

\* \* \* \* \*

#### Item 4. Condensed Financial Information

(a) For all registrants other than money market accounts, furnish the following information for each class of accumulation units of the Registrant, or for such classes of the Registrant and its subsidiaries consolidated as prescribed in Rule 6-03 of Regulation S-X [17 CFR 210.6-03].

\* \* \* \* \*

(b) For each money market account, provide a bar graph showing the annual total returns of the account for each of the last ten fiscal years, or the life of the account if less than ten years. The graph should also show the return for each year in numerical form. Accompany the graph with a statement or statements that: (1) Past performance is not predictive of future performance; (2) money market account performance is primarily affected by short-term interest rates and expenses (and provide a cross-reference to the Registrant's tabular responses to Item 3(a), unless the bar graph and tabular responses to Item 3(a) appear on the same page of the prospectus); and (3) financial statements providing more detailed information regarding the account's performance are

contained in the Statement of Additional Information.

#### Instructions

##### General

Briefly explain the nature of the information contained in the bar graph and that the information is derived from the financial statements in the Statement of Additional Information. The auditor's report as to the financial statements need not be included in the prospectus. Note that the auditor's report as to the fund's financial data reflected in the bar graph is included elsewhere in the registration statement, specify its location, and state that it can be obtained by shareholders.

##### Bar Graph Presentation

1. *Partial Years/New Registrants.* Do not reflect partial fiscal years in the bar graph. The first year shown in the graph will be the first full fiscal year for which: (i) The Registrant's registration statement was effective (or, in the case of a series, the Registrant offered shares of the account); or (ii) the Registrant (or account) invested its assets in accordance with its investment objectives.

2. *Total Return.* Calculate total return as prescribed in Instruction 11 to Item 3(a) of Form N-1A.

3. *Distribution of Capital Gains.* If the account made capital gains distributions during the period, state in a footnote to the graph what the amount of the distribution per share was and state that such distribution is reflected in the bar graph by means of a shaded or otherwise distinctively marked area within the bar for each year in which capital gains distributions were made.

4. *Format.* Measure return on the vertical axis of the bar graph and measure time in yearly increments on the horizontal axis.

5. *Series Companies.* Treat each sub-account as a separate Registrant for purposes of this item.

\* \* \* \* \*

(d) \* \* \*

##### Instruction

A money market account may incorporate its response to this item from the Statement of Additional Information. See General Instruction G.

\* \* \* \* \*

33. Item 5 of Form N-3 (referenced in §§ 239.17a and 274.11b) is amended by revising paragraph (c)(ii), removing paragraph (d), and redesignating paragraph (e) as paragraph (d) to read as follows:

#### Form N-3

\* \* \* \* \*

#### Item 5. General Description of Registrant and Insurance Company

\* \* \* \* \*

(c) \* \* \*

(ii) how the Registrant proposes to achieve its objectives, including:

(A) a short description of the types of securities in which the Registrant invests or will invest principally and, if applicable, any special investment practices or techniques that will be employed in connection with investing in such securities;

(B) if the Registrant proposes to have a policy of concentrating in a particular industry or group of industries, identification of such industry or industries;

(C) the identity of other policies of the Registrant that may be changed only with the approval of a majority of votes, including those policies which the Registrant deems to be fundamental within the meaning of Section 8(b) of the 1940 Act; and

(D) those significant investment policies or techniques (such as risk arbitrage, repurchase agreements, forward delivery contracts, investing for control or management) that are not described pursuant to subparagraphs (A), (B) or (C) above that Registrant employs or intends to employ in the foreseeable future.

#### Instructions

1. In responding to paragraph (c)(ii) of this item (other than paragraph (c)(ii)(B), regarding concentration), it is sufficient for a money market account to:

(a) Describe the characteristics of the account in general terms (e.g., that it seeks to maintain a stable net asset value of \$1.00 by investing in a portfolio of high quality short-term debt obligations, issued by corporations, banks, and other financial institutions, etc.) without listing or describing the particular instruments in which the account may invest or explaining detailed investment policies designed to comply with rule 2a-7 of the 1940 Act; and

(b) If the account limits investment to a group of securities or a type of issuer (e.g., to U.S. government securities), identify: (i) the group of securities or type of issuer and (ii) any other group of securities of type of issuer in which the fund reserves the right to invest more than 5% of its assets and state the maximum percentage of the fund's assets that may be so invested, unless the account has not invested more than 5% of its assets in those securities within the past year and has no current intention of doing so in the foreseeable future.

2. "Concentration", for purposes of paragraph (c)(ii)(B), is deemed to be 25% or more of the value of Registrant's total assets invested or proposed to be invested in a particular industry or group of industries. Registrant's policy on concentration should not be inconsistent with Registrant's name.

3. Discussion of types of investments that will not constitute Registrant's principal portfolio emphasis, and of related policies or practices, should generally receive less emphasis in the prospectus, and under the circumstances set forth below may be omitted or limited to information necessary to identify the type of investment, policy, or practice. Specifically, and notwithstanding paragraph (c) above:

(a) If the effect of a policy is to prohibit a particular practice, or, if the policy permits a particular practice but the Registrant has not employed that practice within the past year and has no current intention of doing so in the foreseeable future, do not include disclosure as to that policy; and

(b) If such a policy has the effect of limiting a particular practice in such a way that no more than 5% of Registrant's net assets are at risk, or, if Registrant has not followed that practice within the last year in such a manner that more than 5% of Registrant's net assets were at risk, and does not have a current intention of following such practice in the foreseeable future in such a manner that more than 5% of Registrant's net assets will be at risk, disclosure of information in the prospectus about such practice should be limited to that which is necessary to identify the practice.

\* \* \* \* \*

34. Form N-3 (referenced in §§ 239.17a and 274.11b) is amended by adding an instruction following Item 11(c) to read as follows:

#### Form N-3

\* \* \* \* \*

#### Item 11. Purchases and Contract Value

\* \* \* \* \*

(c) \* \* \*

#### Instruction

In responding to sub-item 11(c), a money market account need only state that the accumulation unit value represents a proportionate interest in the net assets of the account.

\* \* \* \* \*

35. Form N-3 (referenced in §§ 239.17a and 274.11b) is amended by adding an instruction following Item 11(d) to read as follows:

#### Form N-3

\* \* \* \* \*

#### Item 11. Purchases and Contract Value

\* \* \* \* \*

(d) \* \* \*

#### Instruction

In responding to sub-item 11(d), a money market account that seeks to maintain a stabilized accumulation unit value need not state the time of day at which the calculation is made. \* \* \*

36. Form N-3 (referenced in §§ 239.17a and 274.11b) is amended by adding an instruction following Item 12(a) to read as follows:

#### Form N-3

\* \* \* \* \*

#### Item 12. Redemptions

(a) \* \* \*

#### Instruction

In responding to paragraph (a), a money market account Registrant need not discuss the timing of unit value pricing but should state how the timing of a redemption request will affect the accrual of dividends.

\* \* \* \* \*

37. Form N-3 (referenced in CFR §§ 239.17a and 274.11b) is amended by adding instruction 3 following Item 19(b) to read as follows:

#### Form N-3

\* \* \* \* \*

#### Item 19. Investment Objectives and Policies

\* \* \* \* \*

(b) \* \* \*

#### Instructions:

\* \* \* \* \*

3. In responding to this item, money market accounts should include descriptions of:

(a) The types of instruments which it purchases or intends to purchase;

(b) The types of issuers that issue the instruments in which it intends to invest;

(c) Significant investment policies or techniques (e.g., forward delivery contracts, repurchase agreements, and standby commitments) that the Registrant employs or has the current intention of employing in the foreseeable future; and

(d) The quality, maturity, and diversity restrictions which pertain to money market account investments, to the extent such descriptions have not been included in the prospectus in response to Instruction 1 to Item 5(c).

\* \* \* \* \*

38. Form N-3 (referenced in §§ 239.17a and 274.11b), paragraph (b) of Item 28, is amended by removing paragraph (16) and redesignating paragraph (17) as paragraph (16).

39. Guide 3 to Form N-3 is amended by removing the word "basic" in the first paragraph and substituting in its place "principal".

40. Guide 3 to Form N-3 is amended by adding a paragraph (unnumbered) after the first (unnumbered) paragraph to read as follows:

#### Guide 3. Investment Objectives and Policies

\* \* \* \* \*

In particular, Registrants with money market accounts are urged to be concise in describing the manner in which such accounts propose to achieve their investment objectives (item 5(c)). A general description of the types of instruments in which a money market account may invest (i.e., short-term, high quality instruments) and the types of issuers that issue the securities in which it may invest (e.g., corporations, banks, etc.) should generally be sufficient. As stated in Instruction 1 to Item 5, listing or describing each type of instrument in which the money market account may invest is not required; however, the registrant should identify those groups of securities or types of issuers in which the account has reserved the right to invest more than 5% of its assets, unless it has not invested more than 5% of its assets in those securities or issuers within the past year and has no current intention of doing so in the foreseeable future. Registrants should omit detailed descriptions of rule 2a-7's requirements and the various NRSROs and the ratings they assign. More detailed responses regarding investment policies and techniques should be provided in the SAI in response to Item 13.

\* \* \* \* \*

41. Guide 4 to Form N-3 is amended by adding a footnote at the end of the first sentence to read as follows:

#### Guide 4. Types of Securities

\* \* \* \* \*

<sup>3</sup> As set forth in instruction 1 to Item 5, money market funds are not required to list or describe the particular instruments in which the fund may invest.

\* \* \* \* \*

42. Guide 4 to Form N-3 is amended by adding a final paragraph to read as follows:

#### Guide 4. Types of Securities

\* \* \* \* \*

If an account holds a material percentage of its assets in securities or

other assets for which there is no established market, there may be a question concerning the ability of the account to make payment within seven days of the date its shares are tendered for redemption. The usual limit on aggregate holdings of illiquid assets by separate accounts is 15 percent of net assets. A money market account is limited to investing less than ten percent of its assets in illiquid securities.<sup>5</sup> An illiquid asset is any asset which may not be sold or disposed of in the ordinary course of business within seven days at approximately the value at which the mutual fund has valued the instrument.<sup>6</sup>

\* \* \* \* \*

43. Guide 5 to Form N-3 is amended by adding a footnote at the end of the first sentence to read as follows:

#### Guide 5. Portfolio Turnover

\* \* \* \* \*

<sup>7</sup> Money market accounts are not required to discuss the effects of portfolio turnover in their prospectuses.

44. Guide 8 to Form N-3 is amended by adding a sentence in the second paragraph (unnumbered) following "and standby commitment agreements.\*", to read as follows, and renumbering sequentially all subsequent footnotes in the guides to Form N-3:

#### Guide 8. Senior Securities, Reverse Repurchase Agreements, and Standby Commitment Agreements

\* \* \* \* \*

\* \* \* Money market accounts should discuss their use of these trading practices in the Statement of Additional Information in response to Item 19 (see Instruction 1 to Item 5(c)(ii) and Instruction 3 to Item 19(b)). \* \* \*

45. Guide 21 to Form N-3 is amended to read as follows:

#### Guide 21. Government Securities

If the registrant is investing in United States Government securities, the prospectus should explain when and to what extent the registrant intends to do so.

If a registrant other than a money market account is investing significantly in United States Government securities on a routine basis, the prospectus should include the following information: (1) The types of Government securities in which the separate account will invest; (2) examples of Government agencies and

instrumentalities in whose securities the separate account will invest; and (3) whether the securities of such agency or instrumentality are (a) supported by the full faith and credit of the United States, (b) supported by the ability to borrow from the Treasury, (c) supported only by the credit of the agency or instrumentality, or (d) supported by the United States in some other way. If the registrant is a money market account, the disclosure described in (1) through (3) above should be placed in the Statement of Additional Information.

If the registrant is a money market account holding itself out as investing in United States Government securities, and the registrant does not invest all of its assets in securities backed by the full faith and credit of the United States Government, the account should not suggest in its prospectus or in its sales material that there is no credit risk associated with the account's investments.

46. Guide 27 to Form N-3 is amended by removing the phrase in the first sentence of the tenth paragraph (unnumbered): "with portfolio securities that mature in one year or less".

\* \* \* \* \*

Dated: July 19, 1995.

By the Commission.

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 95-18243 Filed 7-25-95; 8:45 am]

BILLING CODE 8010-01-P

### 17 CFR Parts 232, 240, 249 and 270

[Release Nos. 34-35991; IC-21217; S7-22-95]

RIN 3235-AG56

#### Money Market Fund Quarterly Reporting

**AGENCY:** Securities and Exchange Commission.

**ACTION:** Proposed rule and rule amendment.

**SUMMARY:** The Commission is proposing a new rule under the Investment Company Act of 1940 that would require money market funds to file quarterly reports with the Commission identifying, describing, and providing valuation information for each security in their portfolios. The reports would be filed electronically through the Commission's EDGAR system. This information would enhance the Commission's ability to monitor money market fund compliance with the federal securities laws, particularly rule 2a-7 under the 1940 Act, the rule that

permits money market funds to use special share pricing and portfolio valuation methods.

**DATES:** Comments on the proposed rule and rule and form amendments must be received on or before September 27, 1995.

**ADDRESSES:** Comments should be submitted in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. All comment letters should refer to File No. S7-22-95. All comments received will be available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, N.W., Washington, D.C. 20549.

#### FOR FURTHER INFORMATION CONTACT:

Martha H. Platt, Senior Attorney, (202) 942-0725, or Joseph E. Price, Deputy Office Chief, (202) 942-0721, Office of Disclosure and Investment Adviser Regulation, Division of Investment Management, 450 Fifth Street, N.W., Washington, D.C. 20549.

**SUPPLEMENTARY INFORMATION:** The Commission is proposing for comment:

(1) Rule 30b3-1 under the Investment Company Act of 1940 [15 U.S.C. 80a-1 *et seq.*] ("1940 Act") that would require money market funds to file with the Commission quarterly reports regarding their portfolio holdings; and

(2) Technical amendments to Regulation S-T [17 CFR 232.301], the Commission's general rules for electronic filings, and rule 12b-25 [17 CFR 240.12b-25] and Form 12b-25 [17 CFR 249.322] under the Securities Exchange Act of 1934 [15 U.S.C. 78a *et seq.*], to accommodate notification of late filings of the quarterly reports.

#### Table of Contents

##### Executive Summary

- I. Background
  - II. Discussion
    - A. Money Market Fund Portfolio Schedule
    - B. Reporting Period
    - C. Appendix J to the EDGAR Filer Manual
  - III. Cost/Benefit Analysis
  - IV. Transition Period
  - V. General Request for Comments
  - VI. Summary of Initial Regulatory Flexibility Analysis
  - VII. Statutory Authority
- Text of Proposed Rule and Form Amendments

#### Executive Summary

The Commission is proposing a new rule under the 1940 Act that would require money market funds ("money funds") to file with the Commission quarterly reports regarding their portfolio holdings (the "Money Market Fund Portfolio Schedule" or "Schedule"). The Schedule would be

<sup>5</sup> See Investment Company Act Rel. No. 13380 (July 11, 1983), 48 FR 32555 (July 18, 1983). See also Investment Company Institute (pub. avail. Dec. 9, 1992).

<sup>6</sup> See Investment Company Act Release No. 14983 (Mar. 12, 1986) [51 FR 9773 (Mar. 20, 1986)].